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Premiums Paid in Contemplation of Death: The High Cost of Premiums

Under § 2035 of the 1954 Internal Revenue Code, transfers of interest in property made by a decedent for a less than adequate consideration and within three years of death are presumptively made in contemplation of death. Consequently, they are includible in the decedent's gross estate.¹ The scope of this provision has been debated and contested both legislatively and judicially. Until the development of a recent court trend, noted and developed in this paper, there has been a fluctuation of tax consequences of certain transactions on a decedent's estate. The transactions under discussion will deal with life insurance premiums.

Where there is no dispute that the premiums were paid or transferred in contemplation of death, the sole question to be explored is what amount should be included in the decedent's gross estate?² Courts confronted with this question have produced conflicting results, sometimes based on justifiable distinctions.

First National Bank of Oregon v. U.S. (hereinafter cited as *Slade*) involved such a question. Here the Court of Appeals³ upheld the District Court's⁴ decision to include in the decedent's gross estate the full amount of the life insurance proceeds. This decision rejected the appellant's contention to include only the dollar amount of the premiums paid.

In 1966 the decedent, Mr. Slade, had his wife sign applications for two twenty-year term insurance policies on his life. The policies were issued to Mrs. Slade as owner and beneficiary. All the premiums were paid by Mr. Slade. Within three years of the issuance, Mr. Slade died. Since there was no dispute that the policies were procured and premiums were paid in contemplation of death § 2035 governs.

Considering this background the question left unanswered is, what is the value of the interest transferred in contemplation of death. In concluding

¹ INT. REV. CODE OF 1954, § 2035 provides:

(a) General Rule—The value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, in contemplation of his death.

(b) Application of General Rule—If the decedent within a period of three years ending with the date of his death (except in case of a bona fide sale for an adequate and full consideration in money or money's worth) transferred an interest in property, relinquished a power, or exercised or released a general power of appointment, such transfer, relinquishment, exercise or release shall, unless shown to the contrary, be deemed to have been made in contemplation of death within the meaning of this section and sections 2038 and 2041 (relating to revocable transfers and powers of appointment); but no such transfer, relinquishment, exercise or release made before such 3-year period shall be treated as having been made in contemplation of death.

² See Rhodes, *Contemplation of Death: The Problem of Life Insurance Premiums*,

24 TAX LAWYER 589, (1971).

³ 488 F.2d 575 (5th Cir. 1973).

⁴ 352 F. Supp. 1157 (D.C. Ore. 1972).

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that the full amount of the proceeds should be included in Mr. Slade's gross estate, the court relied heavily on three cases; *Detroit Bank and Trust Co. v. U.S.*,⁵ *Bel v. U.S.*,⁶ and *Chase National Bank v. U.S.*⁷

The *Detroit Bank* case involved a whole life policy purchased by a trust funded with decedent's money for the specific purpose of purchasing the policy. The *Bel* case involved a one-year accidental death policy in the names of decedent's children, purchased with community funds⁸ of the decedent. In the *Detroit Bank*, *Bel* and *Slade* cases the coverage had been purchased within three years of decedent's death, with his funds and at his instigation. The courts included the full proceeds of the policies in the respective decedent's gross estate.

In the *Slade* case the appellants argued that, since Mr. Slade never really owned the policies, he could not have transferred any interest in them within the three-year period. *Chase National* was used to quiet this argument. Justice Stone speaking for the Supreme Court had stated the following:

Obviously, the word 'transfer' in the statute [§§ 401 and 402 (f) of the Revenue Act of 1921, ch. 136, §§ 401, 402 (f), 42 Stat. 277, 279 taxing the 'transfer' of insurance proceeds at death], or the privilege which may constitutionally be taxed, cannot be taken in such a restricted sense as to refer only to the passing of particular items of property directly from the decedent to the transferee. It must, we think, at least include the transfer of property procured through expenditures by the decedent with the purpose, effected at his death, of having it pass to another. Sec. 402 (c) taxes transfers made in contemplation of death. It would not, we assume, be seriously argued that its provision could be evaded by the purchase of a decedent from a third person of property, a savings bank book for example, and its delivery to the intended beneficiary on the purchaser's death, or that the measure of the tax would be the cost and not the value of the proceeds at the time of death.⁹

The *Slade* court maintained that there was only a formal difference between decedent buying the policy, then transferring it to Mrs. Slade and Mrs. Slade procuring the policy at the urging of Mr. Slade, with his funds.

⁵ 467 F.2d 964 (6th Cir. 1972), cert. denied, 410 U.S. 929 (1973).

⁶ 452 F.2d 683 (5th Cir. 1971), aff'g in part 310 F. Supp. 1189 (D.C. La. 1970), cert. denied, 406 U.S. 919 (1972).

⁷ 278 U.S. 327 (1929).

⁸ *Bel* was a resident of a community property state, Louisiana. Community property is included in a decedent's gross estate only to the extent of the decedent's interest under the local law. See INT. REV. CODE OF 1954 §§ 2033, 2042. This interest is one-half the value of the community property (generally).

⁹ 278 U.S. at 327. This same language was relied upon heavily in *Bel* and *Detroit Bank*. The *Chase* case held the estate tax imposed by §§ 401 and 402(f) to be constitutional as a tax on the transfer of property (and not a direct tax on the property). See *Millikin v. U.S.*, 283 U.S. 15 (1931); *U.S. v. Wells*, 283 U.S. 102 (1931). But see *Gorman v. U.S.*, 288 F. Supp. 225, 228 (D.C. E.D. Mich. 1968) and Rev. Rul. 67-463, 1967-2 CUM. BULL. 329.

Therefore, the gift must necessarily be one of a property interest in the policy.¹⁰ The court seemed to feel that this procedure of having Mrs. Slade apply for the policy at Mr. Slade's urging and with his funds was a form of an illusory transfer and that a testamentary substitute occurs therein. The court stated that the only policy that would support such a formalistic distinction would be to encourage tax evasion, a position which the court undoubtedly is opposed to. The court further elaborated that for the taxpayer to prevail in his argument would also undermine [§ 2035's] statutory goal¹¹ as well as give the term transfer an unduly technical¹² meaning. In *U.S. v. Wells*,¹³ the court said the purpose of § 2035 "is to reach substitutes for testamentary dispositions and thus to prevent the evasion of estate tax."¹⁴ The *Slade* court subsequently adopted this language.¹⁵ *Slade* also pointed out the following:

[to agree with appellant's theory] . . . would create an anomalous exception to section 2035 in the case of life insurance policies. The normal rule under section 2035 is that property transferred in contemplation of death is valued as of the decedent's death, not as of the date the property was transferred. Treas. reg. 20.2035-1(e).¹⁶

Referring to Justice Raum's dissenting opinion in *Coleman v. Commissioner of Internal Revenue*,¹⁷ the court further stated that, if only the tax were imposed upon the premiums this would not reflect the appreciated value of what the premiums purchased—the right to the proceeds.

The court claimed that its determination to include the proceeds in decedent's gross estate does not impermissibly¹⁸ reincarnate the old

¹⁰ See, Rhodes, *Contemplation of Death: The Problem of Life Insurance Proceeds*, 24 TAX LAWYER 589, 591, 596 (1971).

¹¹ 488 F.2d at 577.

¹² *Id.*

¹³ 283 U.S. 102.

¹⁴ *Id.* at 117.

¹⁵ 488 F.2d at 577.

¹⁶ *Id.* 26 C.F.R. 2035-1 (e) (1972):

(e) Valuation. The value of an interest in transferred property includible in a decedent's gross estate under this section (2035) is the value of the interest as of the applicable valuation date. In this connection, see sections 2031, 2032 and the regulations thereunder. However, if the transferee has made improvements or additions to the property, any resulting enhancement in the value of the property is not considered in ascertaining the value of the gross estate. Similarly, neither income received subsequent to the transfer nor property purchased with such income is considered.

It should be noted that choosing the alternate valuation date would have no effect on the amount of insurance includible in decedent's gross estate. See also *Estate of Humphrey v. Comm'r.*, 162 F.2d 1 (5th Cir. 1947), cert. denied 332 U.S. 817, decedent gave his children a cash gift in contemplation of death. The gift had been invested. At decedent's death the gift was worth about one-half its original value. The court held under the 1939 Code, for estate tax purposes the gift was to be valued at the full cash transferred. (Noted 61 HARV. L. REV. 365 (1948)). Note the conflict imposed on § 2035 valuations with the value of premiums transferred for gift tax purposes (Treas. Reg. § 25.2511-1(h)(8) (1973)).

¹⁷ *Estate of Inez Coleman*, 52 T.C. 921, 927 (1969). See text accompanying note 41 *infra*.

¹⁸ 488 F.2d at 578. See note 19 *infra*.

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premium payment test¹⁹ phoenix-like from the language²⁰ of § 2035.

It has been demonstrated how the court analyzed that what actually took place was a transfer of an interest in the policy to be valued at the date of the decedent's demise. Therefore, the court held that the full proceeds of the policy were to be included in the decedent's gross estate. The following discussion will try to shed some light on the evolution of the above holding.

BACKGROUND

§ 2035 dealt with numerous types of transfers. Some transfers have been held taxable; others have not for a myriad of rationale.²¹ The scope of discussion will therefore be limited to the area of insurance premiums. To concentrate upon this area even further, the focus will not be concerned with whether the premiums were paid in contemplation of death, assuming they were,²² but their value includable in the decedent's gross estate.

In *Liebman v. Hassett*,²³ the decedent transferred the policy in contemplation of death, but the transferee paid two annual premiums subsequent to the transfer. The court held that the part of the proceeds proportionate to the premiums paid by the transferee should be excluded from decedent's gross estate. Weight was given to the fact that the insured had "taken out" the policy. This case is cited for a merely historical perspective.²⁴ It also illustrates one of the methods used by the courts and the Code to deal with premiums under § 2035.²⁵

¹⁹ The appellant argued that by the adoption of § 2042 (INT. REV. CODE OF 1954), which eliminated the "premium payment" test, does not permit the inclusion of life insurance proceeds in a decedent's gross estate based on who paid the premiums. This argument was based therefore, on Congressional intent. See note 31 *infra*. The "premium payment" test was found in, INT. REV. CODE OF 1939 § 811(g), as amended by § 404(a) (2) of the Revenue Act of 1942, ch. 619 § 404(a) (2), 56 Stat. 944 (now § 2042 of the INT. REV. CODE OF 1954). The "premium payment" test provided for inclusion in one's estate, life insurance based on who paid the premiums, whether directly or indirectly. See *Coleman*, 52 T.C. 921. See also *Goodson, Are Insurance Proceeds Gifts in Contemplation of Death?* 103 TRUSTS & ESTATES 25, 26 (1965); *Yohlin & Bemze, Some Unsolved Gift and Estate Problems of the Unfunded Irrevocable Insurance Trust*, 41 TAXES 521, 533 (1963); *Brown & Sherman*, note 27 *infra*.

²⁰ 52 T.C. at 923, adopted by *Slade* 488 F.2d at 578.

²¹ See generally *LOWNDES & KRAMER, FEDERAL ESTATE AND GIFT TAXES*, 60-79 (1962) and Supp. 21-27 (1972).

²² Due to insurance being so testamentary in nature, there is a more difficult burden of proof to rebut. Therefore, even in the case of life insurance it is not conclusive that the transfer was made in contemplation of death. See *Hull v. Comm'r.*, 325 F.2d 367 (3d Cir. 1963); *Landorf v. U.S.*, 408 F.2d 461 (Ct. Cl. 1969). But see *Garrett's Estate v. Comm'r.*, 180 F.2d 955 (2d Cir. 1950); *First Trust and Deposit Co. v. Shaughnessy*, 134 F.2d 940 (2d Cir. 1943).

²³ 148 F.2d 247 (1st Cir. 1945) *aff'g* 50 F. Supp. 537 (D.C. Mass.).

²⁴ *Id.* This case arose under § 302 (g) of the Revenue Act of 1926 (which was the predecessor of the present § 2035(a) and is substantially the same but, the "premium payment" test on which it relied has been rejected by § 2042 of the 1954 Code).

²⁵ This was considered "harsh" by some; See note 74 *infra*.

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Revenue Ruling 67-463²⁶ was the first official,²⁷ published position taken by the Internal Revenue Service in 1967. This publication involved premiums paid under § 2035. The position basically followed the formula set out in the preceding *Liebman* case. Revenue Ruling 67-463 ran into a great deal of negative reaction by the courts.²⁸

Gorman v. U.S.,²⁹ rejected ³⁰ Revenue Ruling 67-463 shortly after it was published. Here decedent's wife procured a five-year renewable, convertible policy and held all incidents of ownership at all times. The policy was purchased within one year of decedent's death with the sole premium having been paid by the decedent. The court held that only the actual amount of the premium was taxable to the decedent's estate, therefore this result would support appellant's position in the *Slade* case in which the facts were essentially the same.

The *Gorman* court looked to Congressional intent in eliminating the premium payment³¹ test and concluded that the courts and the govern-

²⁶ 1967-2 CUM. BULL. 329. Generally stated: when a decedent within three years and in contemplation of death, paid premiums on his own life policy and transferred the incidents of ownership more than three years prior to his death, value of a proportionate part of amount receivable as proceeds to those premiums paid by decedent within three years of death is includible in his gross estate under § 2035, with the same result if the transferee originally applied for the insurance. See 3 SW.U.L. REV. 124 (1971).

²⁷ This was not a new position among District Directors. See Brown & Sherman, *Payment of Premiums as Transfers in Contemplation of Death*, 101 TRUSTS & ESTATES 790 (1962); once this position was widely accepted, Brown & Sherman, *supra*; Mannheimer, Wheeler & Friedman, *Gifts of Life Insurance by the Insured*, 13 N.Y.U. INST. FED. TAX. 260, n. 27b (1955); Schwartz, *Life Insurance Planning*, 35 SO. CALIF. L. REV. 11, n. 52 (1961-2).

²⁸ The position of the Internal Revenue Service (Rev. Rul. 67-463) was questioned in the courts not less than twelve times and the Internal Revenue Service lost all those decisions except one (*First Nat'l Bank of Midland, Texas v. U.S.*, 69-1 U.S.T.C., ¶ 12,574 (W.D. Tex. 1968)) which too, was shortly thereafter overturned on appeal (423 F.2d 1286 (5th Cir. 1970)).

²⁹ 288 F. Supp. 222 (D.C. E.D. Mich. 1968), *appeal dismissed per stipulation*. See generally 82 HARV. L. REV. 1765 (1969); 67 MICH. L. REV. 812 (1969); 64 NW. U.L. REV. 116 (1969); 43 TUL. L. REV. 882 (1969). See also 57 A.B.A.J. 475 (1967).

³⁰ Revenue Rulings are not binding on the courts although they can be used as precedents. They are official Internal Revenue interpretations of the Code.

³¹ The majority of the House Ways & Means Comm. justified the elimination of the "premium payment" test (§ 811 (g) of the 1939 Code) by saying that life insurance should be on the same footing with other property, since other property is not taxed to decedent's estate, if he completely parted with the property during his life, merely because he paid the consideration for it, H. Rep. No. 1337, 83 Cong., 2d Sess., A 316, A 317 (1954), U.S. CODE CONG. & ADM. NEWS 1954, 4025. The majority's position was reaffirmed when the Congress rejected a Treasury attempt, in 1957, to introduce a modified form of the "premium payment" test into the Code, H.R. 8381, 85 Cong., 1st Sess. 56 (1957). See *List of Substantive Unintended Benefits and Hardships and Additional Problems for the Technical Amendments Bill of 1957*, item 27, p. 12, transmitted on Nov. 7, 1956 to Subcommittee on Internal Revenue Taxation of the House Comm. on Ways & Means, by Treasury and Staff of Joint Comm. on Internal Revenue Taxation, 288 F. Supp. at 227. But see the minority's view; that life insurance is not like other property since it is testamentary in nature, H. Rep. No. 1337, 83 Cong., 2d Sess. B 14, B 15 (1954). The minority was also fearful that the majority's action would ultimately eliminate taxation for estate tax purposes of life insurance proceeds, *id.*

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ment should not try to reenact the test through administrative tactics.³² The court held the tax should be stipulated at the value of the res transferred, at the time the res was transferred.³³ This meant that only the premium dollar value should be included in decedent's gross estate.

In 1969, *Coleman v. Commissioner of Internal Revenue*³⁴ also rejected Revenue Ruling 67-463 as *Gorman* did. Here the insured's three daughters purchased a policy³⁵ on the life of the decedent more than four years prior to his death. The decedent never transferred or possessed any incidents of ownership in the policy. However, the decedent did pay all of the premiums in contemplation of death. The questions under consideration were—1) What should be included in the decedent's gross estate and 2) What really transferred? The taxpayer argued that the legislature's repeal of the premium payment test was the answer. While the District Court in *Gorman* relied heavily on this very argument, here the Tax Court observed that the repeal of the test under § 2042 has no real bearing on cases arising under § 2035. The *Gorman* result was reached but by different means. The court looked to "what the decedent parted with as a result of her payment of the premium in contemplation of death."³⁶ Giving their conclusion more credence, the court stated that the decedent "held no interest whatsoever in the policy or its proceeds."³⁷ The court recognized that "these payments kept the economic substance of that ownership alive," but believed "the decisive point is that what these payments created or maintained was theirs and not hers."³⁸ The court maintained that there was no constructive transfer³⁹ and held that the only thing actually "diverted from her estate was actual money paid."⁴⁰ It should be noted that there was a strong dissent by four justices.⁴¹

The *Slade* court found that the factual setting presented in *Coleman*, was distinguishable from those presented in *Slade*. As noted, in *Coleman*, the policy was procured prior to the statutory period of § 2035 (b). In

³² 288 F. Supp. at 230.

³³ See text accompanying note 16 *supra*.

³⁴ 52 T.C. 921 (1969).

³⁵ The record did not indicate the type of policy.

³⁶ 52 T.C. at 923.

³⁷ *Id.*

³⁸ *Id.*

³⁹ *Id.*

⁴⁰ *Id.*

⁴¹ They believed that the value on "the date on which the transferred property is to be valued is her death date and not when the premiums were in fact paid." *Id.* at 926 (Tietjens, J.). Therefore the value is not measured by the dollar value of the premiums paid but by the "insurance purchased with those premiums." *Id.* at 927, (Raum, J.), this represents the appreciated value of the premiums. Dawson, J. citing *Chase* says look at the substance of the transfer and you will see that what was actually diverted from decedent's estate were the proceeds of the policy. *Id.* at 928. Simpson, Dawson, Raum and Tietjens, JJ. agree in each of the others dissent. A total of three dissenting opinions were written. *Id.* at 926-8.

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Slade the policy was procured within the three-year period. In both cases all premiums were paid by the decedent until the policy matured. In *Slade* and *Coleman*, at all times the policies were owned by one other than the decedent.

In 1970 *First National Bank of Midland, Texas v. U.S.*⁴² was decided. Here the Fifth Circuit⁴³ reversed a lower court decision favoring the Government.⁴⁴ The Circuit Court held only the dollar value of decedent's community interest in the premium payments was to be included in his gross estate. The circumstances were similar to that of *Coleman*. The decedent made all premium payments. Decedent's daughters took out the policies, some seven years prior to his demise. The court emphasized the fact that decedent never had any ownership in the policies. The court said, "the daughters could have paid the premiums themselves; they were under no duty to allow someone else to pay them."⁴⁵ The court agreed with *Coleman*, that the rights maintained belonged to the owners (i.e. the daughters). The court also agreed with *Gorman* in that the authorities cited⁴⁶ to support Revenue Ruling 67-463, do not support the conclusion reached.⁴⁷ In contrast to *Slade*, the same distinguishable facts appear here as they did in *Coleman*.

Because of this lack of success⁴⁸ on the part of the Government, it was indeed time for a new position. Revenue Ruling 71-497⁴⁹ was issued thereby revoking Revenue Ruling 67-463. Revenue Ruling 71-497 using examples, made only premiums paid in contemplation of death on whole life policies includable in a decedent's gross estate where the policies were transferred by the decedent more than three years prior to his death,⁵⁰ with the same effect if it were a five-year term policy. Another example is given to illustrate that the proceeds on a one-year accidental death policy transferred⁵¹ nine months before the accidental death

⁴² 423 F.2d 1286 (5th Cir. 1970).

⁴³ This was the first time a question involving Rev. Rul. 67-463 was to be decided by a Federal Circuit court.

⁴⁴ 69-1 U.S.T.C., ¶ 12,574 (W.D. Tex. 1968).

⁴⁵ 423 F.2d at 1288.

⁴⁶ *Chase Nat'l v. U.S.*, 278 U.S. 327 (1929). This case involved the question whether the federal estate tax imposed on insurance policies owned by the decedent was a direct tax on the property. *Liebman v. Hassett*, 148 F.2d 1947 (1st Cir. 1945). This case arose under § 302 (g) of the Revenue Act of 1926 and should be discounted since the "premium payment" test which it rested on has been rejected. *Scott v. Comm'r.*, 374 F.2d 154 (9th Cir. 1967). This case is irrelevant in that the underlying issue was the ownership of an insurance policy under California law which depended upon payment of premiums as between the spouses.

⁴⁷ 423 F.2d at 1288.

⁴⁸ See *Eliasberg, Contemplation of Death and the Estate Taxation of Life Insurance: What's Left of the Premium Payment Test*, 111 TRUSTS & ESTATES 690, 743 n. 36 (1972).

⁴⁹ 1971-2 CUM. BULL. 329 (1971).

⁵⁰ See *First Nat'l Bank of Midland, Texas v. U.S.*, 423 F.2d 1286 (5th Cir. 1970); *Gorman v. U.S.*, 288 F. Supp. 222 (D.C. E.D. Mich. 1968); *Coleman v. Comm'r.*, 52 T.C. 921 (1969).

⁵¹ See *Chase Nat'l Bank v. U.S.*, 278 U.S. 327 (1929), supports a broad nonliteral definition of the term "transfer"; see the quote that note 9 *supra*, is cited from.

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would be includable in decedent's gross estate.⁵² It should be recognized that for the first time the Internal Revenue Service is giving effect to different types of policies (i.e. whole life, term and accidental death).⁵³ It should also be recognized that the court house door is still open for litigation in two situations: 1) a whole life policy transferred within three years of death with the premiums paid by decedent in contemplation of death; 2) a term policy as to the above circumstances.

Bel v. U.S. involved a one-year accidental death policy.⁵⁴ The policy was procured by the decedent with his community funds less than a year prior to his unfortunate demise. The decedent's children were the named beneficiaries and the record owners. The District Court,⁵⁵ first finding a contemplation of death transfer, held only the amount of the premiums paid were includable in decedent's gross estate. This holding was based entirely on *Coleman*.

An appeal was taken by the Government to the Fifth Circuit.⁵⁶ The Circuit Court looked at the situation in a different perspective.⁵⁷ The court found no relevance to the legislative repeal of the "premium payment" test, stating, "the taxpayer would have us apply a section of the code dealing with lemons (section 2042), to one pertaining to oranges (section 2035)."⁵⁸ The Appeals Court gave no weight to *Coleman* since there the policy was purchased more than three years prior to death⁵⁹ and stated the following:

Thus, the original contractual rights and ownership of the policy in *Coleman* were created outside the presumptive period, and as the Tax Court noted, those premiums paid in contemplation of death served only to keep 'the economic substance of the ownership alive.' In the instant case, however, the premium paid by the decedent less than one year prior to his death engendered the entire right, title and interest which the decedent's children had in the accidental death policy. Essentially, every stick in the bundle of rights constituting the policy and its proceeds had a genesis within three years of the decedent's death.⁶⁰

⁵² It appears that Rev. Rul. 71-497 might have been encouraged by recognition of the decision in *Bel v. U.S.*, 452 F.2d 683 (5th Cir. 1971). The facts and conclusion of this example are essentially those in *Bel*.

⁵³ See 44 U. COLO. L. REV. 633-36 (1973).

⁵⁴ This is actually a form of a term policy.

⁵⁵ 310 F. Supp. 1189 (D.C. La. 1970).

⁵⁶ 452 F.2d 683 (5th Cir. 1971), *aff'g in part* 310 F. Supp. 1189 (D.C. La. 1970), *cert. denied*, 406 U.S. 919 (1972). Noted in 44 U. COLO. L. REV. 633 (1973).

⁵⁷ The Circuit Court affirmed the District Court's finding of a transfer in contemplation of death.

⁵⁸ 452 F.2d at 690.

⁵⁹ *Id.* at n. 3 the court found *First Nat'l.* to be inappropriate but agreed that in *Gorman*, the facts were indistinguishable but said; the *Gorman* court gave the *Chase* court's interpretation of the term "transfer" a too restrictive meaning which would result in undermining the purpose of § 2035.

⁶⁰ 452 F.2d at 690.

Keeping in mind that while the decedent himself executed the original insurance application and paid, with community funds, all of the premiums, the policies from their inception were owned solely by the decedent's three children.⁶¹ *Bel* concluded that an individual should not be able to circumvent § 2035 by passing the property to another.

Indeed, *Bel* stands for a complete new concept, via the views it sets forth. The court dictated that what was actually transferred by the premium payments of decedent was the right to the proceeds which the premiums bought. Thus *Bel* stood for the proposition that not merely the dollar value of the premiums but the proceeds were transferred in contemplation of death. The court therefore held the entire proceeds of the policy includable in decedent's gross estate.

In *Bel* the term transfer was given a peripheral view by giving it a connotative rather than a denotative definition. This connotative view complies with the implication the Supreme Court made in *Chase*, as to the definition of the term "transfer." *Bel* cited *Chase* for support on this view.

There are only technical factual distinctions between *Bel* and *Slade*. In *Slade* the policy was a twenty-year term type and in *Bel* it was a one-year accidental death policy. All other facts are essentially indistinguishable. Indeed, it has been seen that *Slade* relied heavily on *Bel* and the results in both seem to be correct.

The *Detroit Bank and Trust Company v. U.S.* contemplated by the Sixth Circuit⁶² is a post Revenue Ruling 71-497 decision.⁶³ Here the Circuit Court reversed the lower court⁶⁴ which had relied on *Gorman*, and others,⁶⁵ to include only the dollar amount of the premiums in decedent's gross estate. The Appeals Court⁶⁶ included the full proceeds in decedent's gross estate.

Here decedent created an irrevocable trust for his children six months before his death. The decedent transferred, in contemplation of death, money to the corpus for the purpose of purchasing insurance on his life. The trust was the absolute owner of the policy. The court emphasized the intent of Congress in enacting § 2035 was to tax transfers made in contemplation of death at the estate tax rate rather than at a lower rate. The court took cognizance that, subsequent to the lower court's decision, two developments took place—Revenue Ruling 71-497, and the opinion of *Bel*. The court did not speak any further about Revenue Ruling 71-497

⁶¹ *Id.* at 687.

⁶² 467 F.2d 964 (6th Cir. 1972).

⁶³ Subsequent to the District Court's decision Rev. Rul. 71-497 was issued.

⁶⁴ 338 F. Supp. 971 (D.C. Mich. 1971).

⁶⁵ *Merchantile Trust Co. Nat'l Ass'n. v. U.S.*, 312 F. Supp. 108 (D.C. E.D. Mo. 1970); *Coleman v. Comm'r.*, 52 T.C. 921 (1969).

⁶⁶ *McAllister, C.J.*, dissented for reasons set forth by Judge Freeman in his District Court's decision.

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except, that it reiterates the Government's position here. The court then proceeding to eulogize *Bel*, simply incorporated segments of the *Bel* decision into their own. Giving even more credence to their own holding, the court quotes from *Millikin v. U.S.*⁶⁷ and *U.S. v. Wells*⁶⁸ to illustrate that they are upholding Congressional intent by not giving the term "transfer" a technical meaning. The court unveiled the transaction to show a constructive transfer really did take place, holding such transfer should be taxed at the amount of the proceeds. The right to the proceeds were the interest actually transferred.

The facts present here are slightly distinguishable from *Slade*. Here it appears to have been a whole life policy while in *Slade* a term policy. Here the policy was owned by a trust while in *Slade* it was owned by decedent's wife. Here the premiums were paid from a trust which was comprised of decedent's funds while Mr. Slade directly paid the premiums.

This decision closes one of the court house doors left open by Revenue Ruling 71-497.

CONCLUSION

In response to the question as to value of the interest transferred, three general views have emerged. The first was the proportional formula⁶⁹ view. This view was supported at a time by the court⁷⁰ and Government⁷¹ and later also rejected by court⁷² and Government.⁷³ It was thought to be harsh by some.⁷⁴ Consequently, the second view, form v. substance, for the reasons discussed above gained eminence. This judicially⁷⁵ instilled view was joyously accepted by the taxpayers' estates⁷⁶ and unappreciated by the Government.⁷⁷ Finally, the substance v. form view was adopted. This position was acquiesced to by all⁷⁸ but ardently opposed by the taxpayer's estate.⁷⁹ This came after the cursory⁸⁰ positions taken by the courts and was converse to its previous position.

With the change from the form v. substance view to the substance

⁶⁷ 283 U.S. 15 (1931).

⁶⁸ 283 U.S. 102 (1931).

⁶⁹ See notes 23 and 26 *supra*.

⁷⁰ See *Liebman v. Hassett*, 148 F.2d 247 (1st Cir. 1945).

⁷¹ See notes 26 *supra* and 74 *infra*.

⁷² See text accompanying notes 28, 29, 34 and 42 *supra*. But see note 44 *supra*.

⁷³ See note 49 *supra*.

⁷⁴ See 82 HARV. L. REV. 1765, 1766 (1969); Eliasberg, *Contemplation of Death and the Estate Taxation of Life Insurance: What's Left of the Premium Payment Test?* 111 TRUSTS & ESTATES 690, 743 (1972). But see Eliasberg, *id.* at 693 n. 22, 743.

⁷⁵ See notes 29, 34 and 42 *supra*.

⁷⁶ See note 75 *supra*.

⁷⁷ See notes 44 and 75 *supra*.

⁷⁸ See notes 3, 4, 5, 6 and 49 *supra*. See also note 41 *supra*.

⁷⁹ See notes 3, 4, 5 and 6 *supra*.

⁸⁰ The "substance v. form" position emerged after only about 4 years after the "form v. substance" position gained eminence.

v. form view we see how the courts have caroused 180 degrees in their holdings while dealing with parallel facts.⁸¹ This about-face in a few cases may not be a trend but it is enough to initiate a trend. This trend hopefully will continue to make illusory transfers lustrous, at least to the Treasury.⁸²

One must concur with the results of *Slade* and what it represents. It fills in the remaining missing-link of Revenue Ruling 71-497.⁸³ The *Slade* court found a transfer due to the substance and not the form of the transaction. The transfer of the term policy in contemplation of death resulted in the inclusion of the proceeds of the policy in the decedent's gross estate.

The position the courts have taken, which coincides with Revenue Ruling 71-497, is that a transfer of a life policy within § 2035 will result in the proceeds to be included in decedent's gross estate. This position can be avoided if the transfer was made in contemplation of death with "lady luck" (more than three years prior to death). In such a case only the premiums paid within § 2035 will be included in the decedent's gross estate.⁸⁴

JOEL RICHARD LAVENDER

Realistic Preparation for Life Outside Prison*

Working inmates of North Carolina's Department of Correction receive no pay for their labors, not even the token payment received by prison inmates in most states. Honor grade inmates participating in the Work Release Program are paid for their work. When asked why this situation exists, prison officials usually state that it is due to lack of funds and the fact that inmates are in prison to be punished and not rewarded for their transgressions. Some of the hard-core conservatives maintain that to pay a convict would be coddling criminals and affording them an oppor-

⁸¹ Compare *Slade*, 488 F.2d 575 (5th Cir. 1973), and *Detroit Bank & Trust Co.*, 467 F.2d 964 (6th Cir. 1972), and *Bel v. U.S.*, 452 F.2d 683 (5th Cir. 1971) with *Gorman v. U.S.*, 288 F. Supp. 222 (D.C. E.D. Mich. 1968) and *Merchantile Trust Co. Nat'l Ass'n. v. U.S.*, 312 F. Supp. 108 (E.D. Mo. 1970).

⁸² Large amounts of tax revenues are at stake. In 1972 over 1.6 trillion dollars of life insurance were in force in the U.S. alone. In 1972 the amount of coverage in force increased about 8.2% over 1971 (which increased about 7.3% over 1970). THE WORLD ALMANAC AND BOOK OF FACTS at 1021 (1974), source DIVISION OF STATISTICS & RESEARCH, INSTITUTE OF LIFE INSURANCE.

⁸³ The other missing-link was found in *Detroit Bank*, 467 F.2d 964 (6th Cir. 1972). That case involved a whole life policy. Therefore, whether it be whole life, term or accidental death, if "transferred" within three years in contemplation of death the full proceeds will be taxed to the decedent's gross estate.

⁸⁴ Rev. Rul. 71-497, 1971-2 CUM. BULL. 329 (1971). See *First Nat'l Bank v. U.S.*, 423 F.2d 1286 (1970).

* This essay was written by Terry M. Luce, presently an inmate in the North Carolina correctional system. See comment on Mr. Luce's essay, *infra* at 282.